

Soundwill Holdings

More than one single Soundwill Plaza

to summarize...

- Established 2nd tier property company with primary focus in Causeway Bay
- Defensive measurement of current rental income / EV was fair at 4.78%
- 2012 is the window for 3-year lease renewal subject to substantial rent upside
- Low profile engagement in city redevelopment with project delivery from 2012
- Ticker trading at 0.2x 1H FY12/11A P/B

Established 2nd tier property company in old building assembly business.

Madam Grace Foo founded Soundwill in 1978 that started with old building assembly business. In 1990s, the company extended its business towards property development and property investment. In 1996, the company completed its flagship property, Soundwill Plaza and the company was listed in HK the next year. In 2000s the market was rather difficult for smaller developers, Soundwill earned its major cash income came from property rental income as well as building management services. At the same time, the company also recognized substantial non-cash income since its core investment properties appreciated. Table 1 shows its investment property portfolio by end of Jun 2011.

Table 1. Current investment property portfolio

Building	Location	Total GFA	Revenue 1H2011
Soudwill Plaza	Causeway Bay	246,400 sqf	HK\$95m
Other leasing PPT	HK Island	145,280 sqf	HK\$12m
Advertising billboards	Causeway Bay	n.a.	HK\$9m
Total			HK\$116m

Source: SBI E2-Capital

Defensive measurement of current rental income / EV was fair at 4.78%. For 1H FY12/11A, turnover decreased 40.8% YoY to HK\$145.2m due to presence of property assembly income of HK\$98.3m in 1H FY12/10A. Property leasing, urban infrastructure and building management services made up 80%, 15% and 5% turnover for 1H FY12/11A. Yet, there was a higher gain on fair value change of investment properties of HK\$975.5m for 1H FY12/11A compared to HK\$565.0m a year ago. As such, net profit increased 59.6% YoY to HK\$1,004m. As a reference, we employ a defensive measurement of current rental income / EV to capture the strength of Soundwill rental cash inflow. At HK\$232m rental income and HK\$4,710m EV, current rental income-to-EV was 4.78%.

2012 is the window for 3-year lease renewal subject to substantial rent upside.

On top of this current yield rate, Soundwill is likely to deliver higher yield rate through raising rents in 2012. For instance, while current unit rent for street level of Soundwill Plaza was between HK\$650 to HK\$1,200 per sqf a month, it is reasonably expected to have a HK\$1,000+ raise for the 8,800 sqf area that yields extra HK\$50m-100m income a year. As such, with ~HK\$300m rental income and HK\$4,710m EV, expected rental income-to-EV would be raised to 6.84% for FY12/12F.

Table 2. Soundwill Plaza lease information extracts

	Leasing area	Current unit rental	Renewal 2012
Soudwill Plaza			
Street level (G/F)	8,800sqf	HK\$650 – 1,200	80%
Street level (1/F)	9,500sqf	HK\$220 – 260	100%
Upper levels	228,100sqf	HK\$25 – 35	29%

Source: SBI E2-Capital

Ticker	0878 HK
Rating	Not Rated
Price (HK\$)	7.35
Target Price (HK\$)	n.a.
12m Price Range (HK\$)	6.40-14.32
Market cap. (US\$m)	260.7
Daily t/o (US\$m)	0.23
Free float (%)	31.9

Financial summary

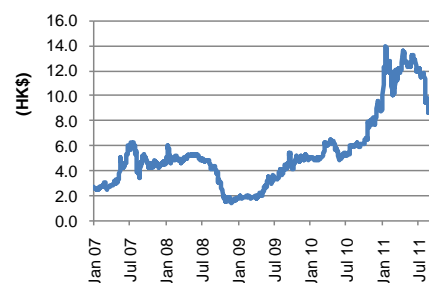
Year to Dec	08A	09A	10A
Turnover (HK\$m)	339.0	713.7	913.7
Net Profit (HK\$m)	162.5	1,058.6	1,732.1
EPS (HK\$)	0.680	4.381	7.090
P/E (x)	10.8	1.7	1.0
P/B (x) pre-CB	0.53	0.35	0.26
EV/EBITDA (x)	22.0	3.8	2.3
Yield (%)	0.95	1.36	1.36
ROE (%)	4.2	18.5	22.3
ROCE (%)	4.2	18.5	22.3
N. Gear. (%)	62.5	34.0	33.5

Source: SBI E2-Capital

	11F	12F	13F
Consensus EPS (HK\$)	1.38	1.65	n.a.
Previous earnings (HK\$m)	-	-	-
Previous EPS (HK\$)	-	-	-

Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	(17.0)	(24.7)	40.9
Actual price changes (%)	(20.0)	(36.3)	11.7



Source: Bloomberg

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Expected acceleration of property assembly business with new compulsory acquisition rule. Besides receiving long-term income from investment properties, with new compulsory acquisition rule effective since Apr 2010 applicable to old buildings aged 50+ year, Soundwill engages in property assembly and development aggressively to gain from 1) short-term income from disposal of land site upon successful acquisition; 2) medium-term income from sales of residential projects in downtown area of Hong Kong Island. Soundwill has a team of 50 staff with extensive local network and experience that facilitates acquisition of old buildings from individuals. Table 3 shows portfolio of property assembly segment. In 2010, 3 land sites were disposed at HK\$591.3m with segment profit of HK\$183.5m representing an EBIT margin of 31%. For 1H 2011, while there was no contribution from this segment, sales of Merlin Street and Hing Wan Street land site should yield HK\$459m and HK\$90m in 2H on top of rental income from its investment properties, while others land sites should contribute after self-development from next year, depending on the opportunities that present itself in the local property market.

Table 3. Portfolio of property assembly segment

	Time	Location	Site area	Planned GFA	Sales	Status
<u>Booked land site sales</u>						
Lin Fa Kung Street West	Jan 2010 disposed	Tai Hang	1,900 sqf	n.a.	HK\$98.3m	Sold and booked
Electric Road	May 2010 disposed	Tin Hau	2,100 sqf	n.a.	HK\$168m	Sold and booked
Sand Wai Street	Sep 2010 disposed	Hung Hom	7,300 sqf	n.a.	HK\$325m	Sold and booked
<u>Projects in progress</u>						
Haven Street	May 2010 acquired	Causeway Bay	12,900 sqf	103,200 sqf (R)	n.a.	R+C self-development
Tang Lung Street	Oct 2010 acquired	Causeway Bay	12,500 sqf	148,800 sqf	n.a.	C self-development
Sharp / Yiu Wah Street	Nov 2010 acquired	Causeway Bay	3,200 sqf	48,000 sqf	n.a.	C self-development
Merlin Street	Dec 2010 acquired	North Point	5,300 sqf	79,000 sqf	HK\$459m	Hotel sold to be booked
Hing Wan Street	Prior to 2010	Wanchai	1,300 sqf	16,000 sqf	HK\$90m	H
School Street	Sep 2011 acquired	Tai Hang	2,250 sqf	22,500 sqf	n.a.	R+C
Mercury Street	Oct 2011 acquired	North Point	2,574 sqf	38,600 sqf	n.a.	Hotel + C

Source: SBI E2-Capital

Low profile engagement in city redevelopment with project delivery from 2012. Another catalyst for 2012 besides the mentioned land site sales is residential projects development. Table 4 shows 2 residential under developments in HK and 4 projects in China. For the 2 Hong Kong projects, Warren Woods is in a more mature stage while Park Haven is in development stage. According to the management, HK\$1,200m pre-sales of Warren Woods of 92,600 sqf at HK\$13,000 per sqf was already made (except 2 units at top floor) and revenue is to be booked in 2012 when occupation permit (OP) is issued. Operating margin could be 50%+. While for Park Haven, construction is in progress. The management targets to begin pre-sales Q4 and expects construction to be completed by the end of 2013. From 2012 onwards, we believe management would be able to establish residential development segment and contribute large portion of turnover.

Table 4. Residential projects summary

	Location	Planned GFA	Land and construction cost	Sales revenue	Pre-sales status	Completion status
<u>Residential projects in HK</u>						
Warren Woods	Causeway Bay	92,600 sqf	HK\$580m	HK\$1,200m	Completed	OP by Jun 2012
Park Haven	Causeway Bay	103,200 sqf	HK\$1,000m	HK\$2,300m * @HK\$23,000/sqf	Launch Q4 2011	OP by end 2013
<u>Residential projects in China</u>						
Zhuhai project A – 51%	Guangdong	589,000 sqf				Expected 2012
Zhuhai project B – 51%	Guangdong	824,000 sqf				Expected 2014
Zhangzhou project	Fujian	75,000 sqf				Expected 2011
Zhaoqing project – 85%	Guangdong	990,000 sqf				Expected 2012-2013

Source: SBI E2-Capital

Illustration of impact of current residential plan turnover. For illustration purpose, we roughly estimate turnover from rental income, property assembly and property development for the coming 3 years. For rental income, HK\$232m rental income is assumed in 2011 while impact of HK\$50m-100m upward revision upon contract renewal is reflected in FY12/12F. On the other hand, with current working capital support, HK\$500m turnover from property assembly is assumed for FY12/12F and FY12/13F. Under these assumptions, property development should make up ~60% and ~70% total turnover of core turnover for FY12/12F and FY12/13F respectively.

Table 5. Illustration of impact of current residential development plan on turnover

Y/E Dec HK\$m	11F	12F	13F
Rental income	232	300	350
Property assembly	549	500	500
Property development	0	1,200	2,300
Total	691	2,000	3,150

Source: SBI E2-Capital

Financial summary. Table 6 and Table 7 show historical profit and loss summary and balance sheet summary. By end of Jun 2011, Soundwill has HK\$223m bank balances and cash (excluding restricted cash). While steady rental income supports property assembly and residential development segments, it is more desirable to secure additional working capital if the company is to accelerate building project pipeline for future growth and development.

Table 6. Profit and loss summary

Y/E Dec HK\$m	08A	09A	10A	1H 11A
Turnover	339	714	914	145
Cost of sales	(72)	(343)	(446)	(18)
Gross profit	267	371	467	127
Fair value gain on investment properties	(0)	964	1,770	976
Operating expenses and others	(51)	(72)	(85)	(60)
EBIT	216	1,263	2,152	1,043
Finance Costs	(61)	(25)	(28)	(20)
Share of results of a JV / associates	(0)	1	(1)	(1)
EBT	155	1,239	2,123	1,023
Income tax expenses	5	(185)	(384)	(20)
Profit for the year	159	1,053	1,739	1,003
Net profit	162	1,059	1,732	1,004
Reported EPS (HK\$)	0.680	4.381	7.090	3.996

Table 7. Balance sheet summary

Y/E Dec HK\$m	09A	10A	1H 11A
Non-current assets			
Investment properties	7,144	10,062	9,750
Other non-current assets	168	158	163
	7,312	10,220	9,913
Current assets			
Properties held for sale	89	0	449
Properties under development	489	776	2,269
Trade and other receivables	71	163	148
Restricted bank deposit	0	238	227
Bank balances and cash	144	218	223
Other current assets	95	90	66
	887	1,484	3,382
Non-current liability			
	44	50	55
Current liabilities			
Trade and other payables	234	234	234
Deposits received from disposal of properties	29	422	534
Borrowings - repayable within one year	2,104	3,092	3,286
Other current liabilities	15	34	28
	2,383	3,781	4,082
Total Equity	5,772	7,873	9,158

Source: Company data, SBI E2-Capital

Our view and valuation. We believe Soundwill is a long-established property developer with experience and expertise in HK. Unlike other 2nd tier developers, Soundwill demonstrates ability to effectively create land bank at attractive cost through old building acquisitions for self development purpose and re-sales purpose. With strong cash flow support from its investment property, we believe Soundwill is able to focus on property assembly as well as residential development. While construction of Warren Woods is underway, we believe execution risk is reducing. With 4.78% current rental income / EV as defensive base, upside is fair-to-attractive, in our view.

Table 8. Peers comparison

Company name	Ticker	Fiscal Year-end	Mkt Cap (US\$m)	Hist P/E (x)	1-yr fwd P/E (x)	2-yr fwd P/E (x)	P/B (x)	ROE (%)
Sounwill Holdings	878 HK	12/2010	260.7	0.8	5.3	4.5	0.2	30.1
Richfield Group	183 HK	06/2011	175.0	8.5	n.a.	n.a.	0.9	12.4

Source: Bloomberg, SBI E2-Capital

Shareholders. Founder and Chairperson Madam Grace Foo owns 68.2% shares in the company. While there is no other single substantial shareholder with 5%+ shareholders, investors such as ASM Asia, Doric Capital Corp, Insight China Focus Fund and Ajia Partners subscribed for Soundwill's shares during placement between Nov 2010 and Apr 2011, totally 11.5m shares out of 274.9m shares.

Table 9. Shareholders of Soundwill

	Shareholding (%)
Chairperson Foo Kam Chu, Grace	68.2
Public	31.8
Total	100.0

Source: SBI E2-Capital

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SELL : absolute downside of >10% over the next six months

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